Big Promises Bump

New President Won't Have an Easy Time Paying for New Initiatives, Fiscal Experts Say

By Lori Montgomery
Washington Post Staff Writer
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On the presidential campaign trail, Democrat Barack Obama promises to "completely eliminate" income taxes for millions of Americans, from low-income working families to senior citizens who earn less than $50,000 a year.

Republican John McCain vows to double the exemption for dependents and slash the corporate income tax.

To which the folks who monitor the nation's financial situation can only say: Good luck. Because, back in Washington, tax collections are slowing, the budget deficit is rising, and the national debt is approaching $10 trillion. Whoever wins the White House this fall, fiscal experts say, is likely to have a tough time enacting expensive new initiatives, be they tax cuts or health care reform.

Economists expect the deficit to top $400 billion when the fiscal year ends Sept. 30, rivaling the all-time high of $413 billion set in 2004. Meanwhile, Congress recently adopted a spending plan that projects a $340 billion deficit in 2009 -- a number likely to grow, lawmakers say, as the cost of the Iraq war rises, the economy weakens and the flow of revenue slows.

Against that dour financial backdrop, the next president will have to decide what to do with President Bush's signature tax cuts, which are due to expire at the end of 2010. Obama and McCain have both promised to keep at least some of them, but that would increase the deficit by $150 billion a year or more. Preventing the alternative minimum tax, or AMT, from expanding to the middle class would add billions more.

Meanwhile, the first baby boomers started receiving Social Security checks in January. Without major policy changes, Medicare and Medicaid are projected to devour half of all federal spending by 2050. But the more immediate problem is the depletion of excess cash in the Social Security trust fund, which has been used for years to cover a portion of the annual budget deficit. Government economists predict that the Social Security surplus will start shrinking in 2011 and dry up completely by the end of the next decade, exposing government-wide budget deficits of a magnitude not seen since Bush's first term.

In a new paper titled "Facing the Music: The Fiscal Outlook at the End of the Bush Administration," University of California at Berkeley economist Alan Auerbach and two co-authors from the Brookings Institution conclude that, if spending grows at historic rates, simply keeping the Bush tax cuts and halting the spread of the AMT would drive the budget deficit to $481 billion by the end of the next president's first term, or 2.7 percent of the economy. Subtract the cash borrowed from Social Security and other retirement funds, and it would be $796 billion, or 4.4 percent of GDP.

"It's a train wreck," said Rep. Paul D. Ryan (R-Wis.), a member of the House Budget Committee. "The government is making promises to people right now it knows it can't keep. And you have some candidates piling more promises on top, which are clearly unfulfillable."

Former House Budget Committee chairman Leon Panetta, who served as President Bill Clinton's first budget director, said the financial situation is "much worse" than it was in 1993, when Clinton was forced to abandon promises of a middle-class tax cut before he took office. Instead, Clinton wound up devoting his first State of the Union address to a plan that aimed to tame rising deficits with one of the largest tax hikes in history.

"It's worse because there are a huge number of crises out there that are going to confront the new president," Panetta said, citing costly wars in Iraq and Afghanistan alongside the rising cost of Social Security and Medicare. "We're looking at a $400 billion deficit this year with the economy in recession or near recession. The likelihood is that it's going to get worse. And the fundamental problem has been that there's very little willpower by Republicans or Democrats to confront the issue."

A commitment by congressional Democrats to follow pay-as-you-go budget rules could further complicate the next president's ability to pursue expensive initiatives.

Obama has not made balanced budgets a priority. Instead, he promises numerous tax cuts likely to make the situation worse, including subsidies for education, child care, homeownership, "savers" and people who work. Obama also vows to extend the Bush tax cuts for families who earn less than $250,000 a year. According to an analysis by the Tax Policy Center, a joint project of Brookings and the Urban Institute, his tax plans would deprive the Treasury of nearly $900 billion in his first term, and increase the national debt by $3.3 trillion by 2018.

That analysis excludes some expensive proposals, including promises to close the gap in prescription drug coverage for Medicare recipients (estimated to cost about $400 billion over 10 years); to introduce government-funded health insurance for the uninsured (which the campaign estimates would cost as much as $65 billion a year); and to make large-scale investments in energy, education and infrastructure, which Obama dubbed his "competitiveness agenda" during a speech this week in Flint, Mich.

The analysis also excludes a possible reduction in corporate tax rates, which Obama first mentioned in an interview this week with the Wall Street Journal. Campaign officials said Obama would pay for the rate reduction by closing corporate tax loopholes.

Obama economic adviser Austan Goolsbee said the senator has identified ways to cover the costs of his proposals, starting with savings of $90 billion a year from ending the Iraq war. "All of his programs are paid for and the deficit would come down" from where it is today, Goolsbee said.

McCain has proposed even bigger tax reductions, including an extension of all the Bush tax cuts, permanent limits on the AMT and a 10 percent reduction in the corporate tax rate. All told, McCain's tax plans would cost the Treasury more than $1.1 trillion during his first term, and would increase the national debt by $4.3 trillion by 2018, according to the Tax Policy Center analysis.

McCain does vow to balance the budget, but he proposes to do it by slashing spending projections for troops abroad, domestic programs and health care -- reductions unlikely to pass muster with a Democratic Congress.

"They're promising the world with ways to pay for it that are really suspect," Bob Williams, one of the authors of the Tax Policy Center study, said of both candidates.

Despite his promises of tax cuts, fiscal analysts note that McCain has a reputation as a budget-cutter. He voted against the Bush tax cuts he now proposes to extend and refuses to request funding for local programs known as earmarks. He has been talking about the need to reform Social Security, Medicare and Medicaid since the race began more than a year ago.

"I suspect that McCain will be more constrained and will have a veto power over the Democratic Congress," said Alice M. Rivlin, who served as the first director of the Congressional Budget Office, as well as one of Clinton's budget directors. "If it's Obama, the Democratic Congress is going to be pushing for spending and it's awfully hard to rein in your own folks. No Democrat is going to want to go to war with Congress."

Budget experts also note that progress on the deficit has often come with divided government because both parties can shoulder blame equally. And there is likely to be plenty of blame to go around if the candidates make good on their promise to tackle long-term deficits in the retirement programs. Few options are likely to be popular with voters: Obama has discussed raising the cap on the Social Security payroll tax, hitting higher-income families with another tax hike. McCain has proposed charging wealthy seniors higher premiums for Medicare prescription-drug benefits.

G. William Hoagland, who worked for years as a budget adviser to top Senate Republicans, predicted that the nation's money troubles will be a painful and persistent headache for whoever next occupies the White House. "The platter is so full for the next president," Hoagland said, "I think at some point the reality will start to set in that there have been a lot of promises made that aren't going to be addressed very quickly."